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IN THE

Supreme Court of the United States

CENTRAL VIRGINIA COMMUNITY COLLEGE,
VIRGINIA MILITARY INSTITUTE,
NEW RIVER COMMUNITY COLLEGE, and
BLUE RIDGE COMMUNITY COLLEGE,

Petitioners,

v.

BERNARD KATZ, Liquidating Supervisor of the Bankruptcy Estate in *In re Wallace's Bookstores, Inc.*,

Respondent.

ON WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SIXTH CIRCUIT

BRIEF FOR THE RESPONDENT

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QUESTIONS PRESENTED

1. Whether a state agency's filing of a proof of claim and participation in a bankruptcy case waives the State's sovereign immunity with respect to a preference action to recover funds that the State or its agencies have no right to retain and that may be administered as part of the bankruptcy estate.

2. If Petitioners' claim of sovereign immunity is not waived, whether the Eleventh Amendment bars a preference action brought by a court-appointed official supervised by the Department of Justice on behalf of a federally created bankruptcy estate to recover funds that the State or its agencies have no right to retain and that may be administered as part of the estate.

3. If Petitioners' claim of sovereign immunity is not waived, whether the Eleventh Amendment bars a bankruptcy court from exercising *in rem* jurisdiction to determine title to funds received by a state agency and to recover the funds that the agency has no right to retain and that may be administered as part of the estate.

4. If Petitioners' claim of sovereign immunity is not waived, whether Petitioners lack a defense of sovereign immunity because in ratifying the Constitution the States ceded their immunity with respect to the administration of uniform bankruptcy proceedings.

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BRIEF FOR RESPONDENT

This matter arises out of the chapter 11 bankruptcy case of Wallace's Bookstores, Inc. ("Wallace"). Petitioners are Virginia Military Institute ("VMI"), Central Virginia Community College ("Central"), New River Community College ("New River"), and Blue Ridge Community College ("Blue Ridge"). Petitioners contend that, "[l]ike all public institutions of higher education in Virginia, [Petitioners] are considered the Commonwealth [of Virginia] for purposes of sovereign immunity." Pet. Br. at 1 n.1. Petitioners are represented by their counsel, Virginia Attorney General Judith Williams Jagdmann. *Id.* at 1. Respondent is Bernard Katz ("Katz" or "Respondent"), the court-appointed liquidating supervisor for Wallace's bankruptcy estate.

STATEMENT

A. General Background and Wallace's Bankruptcy Filing

Prior to filing for bankruptcy, Wallace operated a chain of college bookstores, and supplied new and used textbooks for students. Wallace did business with each of the Petitioners, including operating campus bookstores at VMI, Central, Blue Ridge, and New River. On February 28, 2001, Wallace commenced its bankruptcy case by filing a petition for relief under chapter 11 the Bankruptcy Code, 11 U.S.C. §§ 101, *et seq*.

By operation of federal law, when a debtor commences a bankruptcy case, a bankruptcy estate is created consisting of all of the debtor's property wherever located. 11 U.S.C. § 541. Likewise, the federal court in which the case is commenced is vested with exclusive *in rem* jurisdiction over all property of the bankruptcy estate, and the estate is formed *in custodia legis*. 28 U.S.C. § 1334(e); *Tennessee Student Assistance Corp. v. Hood*, 541 U.S. 440, 447 (2004); *Straton v. New*, 283 U.S. 318, 320-21 (1931). Accordingly, if a governmental entity has seized possession of property in which the estate has an interest before the debtor commences its bankruptcy case, the bankruptcy court may direct the entity to relinquish possession of the property to

the representative of the estate so that it may be administered as part of the estate. *United States v. Whiting Pools*, 462 U.S. 198, 211 (1983). In this case, after Wallace filed its chapter 11 petition, all of its property became vested in its bankruptcy estate to be administered as prescribed by the Bankruptcy Code.

The filing of a bankruptcy petition also triggers the "automatic stay," which enjoins all debt collection activity against the debtor and property of the estate during the bankruptcy proceeding. 11 U.S.C. § 362(a). In accordance with the automatic stay, Wallace's filing of its bankruptcy case prevented any of the Petitioners from taking action to collect their claims against Wallace or property of its estate.

B. VMI's Proof of Claim and the Proofs of Claim filed by other Virginia Educational Entities

Under the Bankruptcy Code, a debtor's monetary obligations constitute "claims" against the debtor's estate, and a creditor holding a pre-petition claim is entitled to file a "proof of claim" with the bankruptcy court. 11 U.S.C. §§ 101(5), 101(10), 501(a), 502(b); Fed. R. Bankr. P. 3001, 3002; *see Katchen v. Landy*, 382 U.S. 323, 336 (1966) ("bankruptcy . . . converts the creditor's legal claim into an equitable claim to a pro rata share of the *res*").[1] Only creditors (including state entities) that file proofs of claim may receive distributions from the debtor's bankruptcy estate. Fed. R. Bankr. P. 3002(a); *New York v. Irving Trust Co.*, 288 U.S. 329, 333 (1933).

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[1] The Bankruptcy Code defines "creditor" as a person holding a claim that arises before the debtor commences a bankruptcy case. 11 U.S.C. § 101(10). The term "creditor" specifically includes a "governmental unit." 11 U.S.C. §§ 101(15), 101(27). The term "pre-petition" refers to claims or events arising or occurring *before* the debtor files a bankruptcy petition. Conversely, the term "post-petition" refers to claims or events arising or occurring *after* the debtor files.

In this case, on July 6, 2001, Petitioner VMI filed a proof of claim with the bankruptcy court asserting a claim of $43,237.60 against the estate.[2] In addition, on April 9, 2001, the Darden Graduate School of Business at the University of Virginia filed a proof of claim, and on June 25, 2001 filed two other proofs of claim.[3] On May 2, 2001, the Weldon Cooper Center for Public Service at the University of Virginia filed separate proofs of claim in the amounts of $1,038.80 and $155.76.[4] On June 19, 2001, Christopher Newport University filed a proof of claim in the amount of $869.03.[5] Numerous other creditors, including agencies of other States, also filed proofs of claim.

C. Wallace's Sale of its Bookstore Assets

Immediately after Wallace commenced its bankruptcy case, Wallace continued to operate its business as a "debtor in possession." 11 U.S.C. §§ 1101(1) (defining "debtor in possession" in a chapter 11 case), 1107 (prescribing duties of debtor in possession, including duties of trustee), 1108 (authorizing operation of business). On March 13, 2001, the Office of the United States Trustee – a division of the Department of Justice with oversight authority in bankruptcy cases – appointed a committee of unsecured creditors to take part in the administration of the case. 11 U.S.C. § 1102; *see* 28 U.S.C. §§ 581, *et seq.* Thereafter, in conjunction with the

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[2] *See In re Wallace's Bookstores* (Bankr. E.D. Ky.) Case Nos. 50545 through 50606 (jointly administered) (the "Bankruptcy Case"), Claim No. 2748.

[3] *See* Bankruptcy Case Claim Nos. 148 ($1,297.31), 1251 ($1,297.28), 1252 ($1,297.28).

[4] *See* Bankruptcy Case Claim Nos. 247 ($1,038.80), 248 ($155.76).

[5] *See* Bankruptcy Case Claim No. 839 ($869.03).

creditors' committee, Wallace determined to sell its assets as the best means to maximize the value of its bankruptcy estate.

On April 10, 2001, the bankruptcy court entered an order approving bidding procedures for the sale of the estate's bookstore assets. *See* 11 U.S.C. § 363(b) (authorizing a bankruptcy court to approve the disposition of the estate's property). These included bookstores located at Central (the "Central Store"), VMI (the "VMI Store"), Blue Ridge (the "Blue Ridge Store") and New River (the "New River Store").[6] At the conclusion of the bidding process, the Follett Corporation ("Follett") was the high bidder for the Blue Ridge Store and the New River Store. Barnes and Noble College Bookstores, Inc. ("Barnes & Noble") was the successful bidder for the VMI Store and the Central Store.

By order dated May 18, 2001, the bankruptcy court approved Follett's bid and ordered Follett to use its best efforts to negotiate agreements with Blue Ridge and New River to effect a transition between Wallace and Follett at the Blue Ridge Store and the New River Store.[7] Both Blue Ridge and New River participated in the process and the transition of the stores at their campuses to Follett. On June 4, 2001, the bankruptcy court entered a similar order approving the sale of the VMI Store to Barnes & Noble.[8] VMI participated in this process by, *inter alia*, indicating a preference for Barnes & Noble as the successor operator for its bookstore. The bankruptcy court likewise approved the sale of the Central Store to Barnes & Noble.[9]

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[6] *See* Bankruptcy Case Docket No. 224.

[7] *See* Bankruptcy Case Docket No. 404.

[8] *See* Bankruptcy Case Docket No. 440.

[9] Another Virginia educational institution, Northern Virginia Center, also actively participated in the sale of the Wallace bookstore located on its campus to Barnes & Noble.

Petitioners obtained significant benefits from Wallace's administration in chapter 11 and their participation in the court-supervised disposition of Wallace's bookstore assets. Among other things, Petitioners enjoyed the orderly transition of operations from Wallace to either Follett or Barnes & Noble without interruption of services to students at their campuses, and without the delay associated with the procedures typically required for the provisions of services to public institutions of higher education in Virginia under the Virginia Public Procurement Act. *See* Va. Code §§ 2.2-4300, *et seq.*

D. Wallace's Chapter 11 Plan and the Bankruptcy Court's Appointment of Respondent Katz to Serve as Trustee of the Estate

On May 20, 2002, the bankruptcy court confirmed Wallace's Amended Joint and Consolidated Plan of Liquidation (the "Plan").[10] *See* 11 U.S.C. §§ 1129 (providing for the confirmation of chapter 11 plans), 1141 (prescribing the effect of confirmation of a plan). Pursuant to the Plan, on May 30, 2002, the bankruptcy court appointed Respondent as Liquidating Supervisor of Wallace's bankruptcy estate. The court appointed Respondent to serve as trustee of the estate and to represent the estate; to resolve claims against the estate; to collect uncollected assets; to liquidate the estate's property; and to distribute the proceeds equitably among creditors as provided under applicable bankruptcy law. *See* 11 U.S.C. § 323(a).[11]

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[10] *See* Bankruptcy Case Docket No. 1095.

[11] *See also* Article VI of the Plan, Bankruptcy Case Docket No. 969 (prescribing Respondent's duties).

E. The Claims-Allowance and Adjustment Process, and Petitioners' Preference Obligations

The filing of a proof of claim with the bankruptcy court – such as VMI's filing of its proof of claim in this case – implicates the Bankruptcy Code's claims-allowance and adjustment procedures. Pursuant to section 501(a) of the Code, a claim is deemed "allowed," and therefore entitled to participate in distributions from the estate, if no party in interest objects to the claim. 11 U.S.C. § 502(a). Pursuant to section 502(b), if an objection to a claim is filed, the bankruptcy court is required to resolve the objection and either allow or disallow the claim. Pursuant to section 502(d), the bankruptcy court must disallow a claim if the creditor asserting the claim owes unsatisfied obligations to the bankruptcy estate, including any "preference" obligation under section 547 of the Code. 11 U.S.C. § 502(d) ("the court shall disallow any claim of any entity. . . that is a transferee of a transfer avoidable under section . . . 547 . . . of this title, unless such . . . transferee . . . has . . . turned over any such property"); *see Keppel v. Tiffin*, 197 U.S. 356, 363-64 (1905) (explaining operation of predecessor to section 502(d)).

Section 547 governs the determination of preferences and provides that a trustee may "avoid" any transfer to a creditor that the debtor made within 90 days before the debtor's bankruptcy case that enabled the creditor to receive a larger percentage of its claim than the creditor would receive as a distribution through the bankruptcy process. 11 U.S.C. § 547(b); *see Union Bank v. Wolas*, 502 U.S. 151, 154-55 (1991); *Begier v. IRS*, 496 U.S. 53, 58 (1990). In turn, section 551 of the Code automatically preserves for the benefit of the estate a transfer avoided under section 547. 11 U.S.C. § 551 ("Any transfer avoided under section . . . 547 . . . is preserved for the benefit of the estate.").

Pursuant to section 542 of the Code, the transferee of property that may be administered as part of the estate is obligated to return the property to the estate. 11 U.S.C. § 542(a)

("an entity . . . in possession, custody, or control . . . of property that the trustee may use . . . shall deliver to the trustee . . . such property"). In turn, section 550 permits the trustee to recover the transferred property for the benefit of the estate. 11 U.S.C. § 550(a).

As this Court has observed, the preference provisions serve two purposes. First, they promote the central bankruptcy policy of equality of distribution among creditors. *Wolas*, 502 U.S. at 160-61; *Begier*, 496 U.S. at 58. Second, they discourage debt collection activity against the debtor while the debtor struggles on the verge of bankruptcy by requiring the creditor to disgorge the fruits of its collection activities. *Wolas*, 502 U.S. at 160-61.

In this case, each Petitioner received significant preferential payments from Wallace just before Wallace filed for bankruptcy and none has returned its preferential payments to the estate.[12] Accordingly, Katz objected to VMI's proof of claim under section 502(d) and commenced adversary proceedings in the bankruptcy court against Petitioners to recover the preferential payments that each received. J.A. at 2-35.[13]

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[12] VMI received $25,595.00, J.A. at 6; New River received $65,264.00, J.A. at 33; Central received $63,387.00, J.A. at 15; and Blue Ridge received $34,054.58, J.A. at 23.

[13] Katz also asserted additional claims against Petitioners in two groups: (1) claims against VMI and Blue Ridge under section 544 of the Code and a state statute that permits the recovery of certain payments, Ky. Rev. Stat. Ann. § 378.060 (Michie 2004), and (2) claims for certain unpaid debts owed to Wallace. Katz voluntarily dismissed the first group of claims after this Court granted certiorari. Katz has moved voluntarily to dismiss the second group of claims, leaving only the preference actions. Petitioners have indicated that they may object to dismissal of the second group of claims. The dismissal of the additional claims does not affect the issues presented to this Court.

F. Disposition in the Courts Below

Petitioners moved to dismiss the four preference proceedings on the ground that the actions are barred by the doctrine of sovereign immunity. In response, Katz argued, *inter alia*, that Petitioners had waived any sovereign immunity by VMI's filing of its proof of claim. *See, e.g.*, J.A. at 45. Relying on the Sixth Circuit's decision in *Hood v. Tennessee Student Assistance Corp.*, 319 F.3d 755 (6th Cir. 2003), the bankruptcy court denied Petitioners' motion to dismiss. Petitioners appealed the bankruptcy court's denial to the district court, and Respondent again asserted his waiver argument. The district court affirmed the bankruptcy court on the basis of the Sixth Circuit's decision in *Hood*. J.A. at 44-45. Petitioners then appealed to the Court of Appeals.

While Petitioners' appeal was pending, VMI attempted to withdraw its proof of claim "to the extent the proof of claim constitutes a waiver of sovereign immunity."[14] The bankruptcy court declined to grant the motion. On May 17, 2004, the Court issued its decision in *Tennessee Student Assistance Corp. v. Hood*, 541 U.S. 440 (2004). Since that time, VMI has not pursued further its motion to withdraw its proof of claim. *Cf. Bronx Brass Foundry, Inc., v. Irving Trust Co.*, 297 U.S. 230, 231-32 (1936) (affirming bankruptcy court's refusal to permit withdrawal of proof of claim). Three months after this Court issued its opinion in *Hood*, the Sixth Circuit affirmed the district court in an unpublished *per curiam* opinion. J.A. at 46-47. This appeal followed.

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[14] VMI made two separate motions to withdraw its proof of claim, one in the adversary proceeding, Bankruptcy Case Docket No. 1632, and an amended motion in the bankruptcy case itself, Docket No. 1634.

SUMMARY OF ARGUMENT

Petitioners argue that the preference adversary proceedings brought by Katz offend Virginia's sovereign immunity. Virginia, however, waived its sovereign immunity when VMI and various other state institutions – which are considered to be Virginia for purposes of sovereign immunity – invoked the federal bankruptcy court's jurisdiction by filing proofs of claim and by participating in the case. As this Court has long recognized, a State may waive its sovereign immunity by participating through one of its agencies in a federal court proceeding, and in particular does so by filing a proof of claim with a federal bankruptcy court. So, too, in this case, Virginia has waived any claim of sovereign immunity.

Even in the absence of a waiver, Virginia cannot invoke sovereign immunity because the proceedings at issue are not brought by a private citizen of any State against one of the States. Rather, the actions are brought by the court-appointed representative of a federally created entity exercising authority under the laws of the United States and operating under the supervision of the Department of Justice. Just as a State has no immunity from a suit brought against it by the United States, Virginia has no defense of sovereign immunity to the proceedings at issue here.

In addition, the State's defense of sovereign immunity does not apply because the recovery of a preference lies within the *in rem* authority of the bankruptcy court to recover property that the State, under federal law, has no right to keep. A State has no authority to refuse the superior right of the bankruptcy estate under federal law to property that can be administered as part of the bankruptcy proceeding. Accordingly, Petitioners may be compelled to return the payments that they received.

Finally, the State's defense of sovereign immunity does not apply because, in adopting the Constitution, the States ceded

their immunity from the application of uniform federal bankruptcy rules, including those regarding title and possession of property to be administered as part of the bankruptcy estate. The recovery of preferential payments has been a part of the fabric of bankruptcy law since before the signing of the Constitution. If preferences cannot be recovered from state entities that have received them, then there is no way to enforce this critical and longstanding feature of bankruptcy law and States may disregard this aspect of bankruptcy law with impunity. This would render the federal bankruptcy law non-uniform in violation of the Constitution by, among other things, shielding from its reach state entities that manage to extract payment from a debtor before the debtor files for bankruptcy, while leaving the United States and state entities that have not received payment to abide the bankruptcy law in order to receive distributions on their claims.

ARGUMENT

A. Petitioners Have Waived Any Claim of Sovereign Immunity.

1. The Court should consider Respondent's waiver argument.

Petitioners contend that Congress lacks the authority to abrogate a State's immunity from suit through the exercise of its Article I powers, and, therefore, that section 106 of the Bankruptcy Code, which explicitly renders the States subject to certain proceedings under the Code, is unconstitutional. This Court's "settled policy," however, is to avoid the decision of constitutional issues where doing so is not necessary to the resolution of a pending case. *Nixon v. Fitzgerald*, 457 U.S. 731, 748 n.27 (1982); *see Hood*, 541 U.S. at 454-55 (citing *Liverpool, New York & Philadelphia S.S. Co. v. Commissioners of Emigration*, 113 U.S. 33, 39 (1885) ("[We are bound] never to anticipate a question of constitutional law in advance of the necessity of deciding it")); *Minnesota v. National Tea Co.*, 309

U.S. 551, 557 (1940). In this instance, it is unnecessary to decide the constitutional question that Petitioners raise because, whatever sovereign immunity Virginia might have had, Virginia waived its sovereign immunity when its agencies filed various proofs of claim and otherwise availed themselves of the benefits of the bankruptcy proceedings.

The Court likewise should address Respondent's waiver argument because Respondent raised it below; Petitioners have anticipated and addressed the argument in their brief; and the factual basis for the argument is in the record. *See Washington v. Confederated Bands & Tribes of Yakima Indian Nation*, 439 U.S. 463, 477 n.20 (1979) ("As the prevailing party, the appellee was of course free to defend its judgment on any ground properly raised below whether or not that ground was relied upon, rejected, or even considered by the District Court or the Court of Appeals."). Even if Respondent had not raised his waiver argument below, a prevailing party is nonetheless "entitled to rely on any legal argument in support of the judgment below." *Schiro v. Farley*, 510 U.S. 222, 228-29 (1994); *see also Bennett v. Spear*, 520 U.S. 154, 167 (1997); *Dandridge v. Williams*, 397 U.S. 471, 476 n.6 (1970) ("The prevailing party may, of course, assert in a reviewing court any ground in support of his judgment, whether or not that ground was relied upon or even considered by the trial court."); *Ponte v. Real*, 471 U.S. 491, 500 (1985); *United States v. American Ry. Express Co.*, 265 U.S. 425, 435-36 (1924).

2. A state agency waives sovereign immunity by filing a proof of claim.

The Eleventh Amendment "is rooted in a recognition that the States, although a union, maintain certain attributes of sovereignty, including sovereign immunity." *Seminole Tribe v. Florida*, 517 U.S. 44, 54 (1996) (internal citation omitted). It is inherent in the nature of sovereignty not to be amenable to the suit of an individual without the sovereign's consent. *Id.* Sovereign immunity, however, is not absolute, and a State may

waive it. *Lapides v. Board of Regents*, 535 U.S. 613, 618 (2002); *see also Clark v. Barnard*, 108 U.S. 436, 447 (1883). Waiver generally may arise in one of two ways: the State may make a clear declaration in a statute or contract that it is subject to suit in federal court (waiver by consent), or the State, through an agency, may engage in conduct that surrenders the State's immunity (waiver by conduct). *Lapides*, 535 U.S. at 618; *College Sav. Bank v. Florida Prepaid Postsecondary Educ. Expense Bd.*, 527 U.S. 666, 675-676 (1999). Whether a particular set of state laws, rules, or activities amounts to a waiver of immunity is a question of federal law. *Lapides*, 535 U.S. at 623.

Based on notions of fundamental fairness and judicial consistency, this Court has found a waiver of sovereign immunity by conduct where a State voluntarily invokes the jurisdiction of a federal court. *See Lapides*, 531 U.S. at 618-622; *Porto Rico v. Ramos*, 232 U.S. 627, 631 (1914); *Richardson v. Fajardo Sugar Co.*, 241 U.S. 44, 47 (1916); *Gunter v. Atlantic Coast Lines R. Co.*, 200 U.S. 273, 284 (1906); *Clark*, 108 U.S. at 448. This Court has specifically found a waiver by conduct where a State, through one of its agencies, filed a proof of claim in a bankruptcy case. *See Gardner v. New Jersey*, 329 U.S. 565, 574 (1947). In this instance, VMI and other Virginia agencies filed proofs of claim with the bankruptcy court, thereby invoking the bankruptcy court's jurisdiction and waiving Virginia's immunity with respect to claims adjustments and counterclaims based on the Bankruptcy Code's preference provisions.

Petitioners may argue that a state agency authorized to file a proof of claim is not authorized to waive sovereign *immunity* and therefore does not do so. Such an argument, however, confuses the two distinct methods by which a State may waive immunity (waiver by consent versus waiver by conduct), and the argument was expressly rejected in *Lapides*. In *Lapides*, the Court held that the authorized invocation of federal-court jurisdiction – even without express authority to waive sovereign immunity – is sufficient to waive the State's immunity "because

an interpretation of the Eleventh Amendment that finds waiver in the litigation context rests upon the Amendment's presumed recognition of the judicial need to avoid inconsistency, anomaly, and unfairness, and not upon a State's actual preference or desire, which might, after all, favor selective use of 'immunity' to achieve litigation advantages." 535 U.S. at 620. Moreover, VMI can hardly contend that it was unaware that the filing of a proof of claim implicates the Bankruptcy Code's claims-allowance process and the requirement that preferences be disgorged. As noted, section 502 governs the allowance of claims in bankruptcy, and section 502(d) plainly requires the disallowance of claims if preferential payments have been received and not relinquished. 11 U.S.C. § 502(d).

The Court's decision in *Gardner* leaves no doubt that a State waives sovereign immunity by filing a proof of claim. *Gardner* was a bankruptcy case in which the Comptroller of New Jersey filed a proof of claim for unpaid taxes. The trustee, on behalf of the bankruptcy estate, objected to the State's claim, and petitioned the bankruptcy court to determine either that a tendered compromise of the claim bound the State, or, alternatively, for adjudication of the amount and priority of the State's claim. In response, the State asserted sovereign immunity. *Gardner*, 329 U.S. at 571. Observing that it "is traditional bankruptcy law that he who invokes the aid of the bankruptcy court by offering a proof of claim and demanding its allowance must abide the consequences of that procedure," this Court held that when a State voluntarily invokes the bankruptcy court's jurisdiction by filing a proof of claim, it waives any immunity that it otherwise might have had. *Id.* at 573-74.

Here, Virginia, through VMI and other arms of the State, unequivocally took steps to participate in the distribution of the assets of the estate by filing their proofs of claim, and in doing so submitted to the jurisdiction of the bankruptcy court with regard to the adjudication of their claims and any adjustment or counterclaims arising under the Bankruptcy Code. In varying degrees, each of the Petitioners also availed themselves of the

benefits of the bankruptcy proceedings by participating in the disposition of the VMI Store, the Blue Ridge Store, the New River Store, and the Central Store. Accordingly, Virginia, through its agencies, has waived any Eleventh Amendment immunity that it might otherwise have had with respect to the application of ordinary bankruptcy procedures that apply in the administration of claims, including claims adjustments and counterclaims based upon the Code's preference provisions.

3. A state agency waives the State's sovereign immunity when it files a proof of claim, and this waiver binds all "arms" of the same State.

Petitioners contend that the proofs of claim filed by VMI and other Virginia educational institutions do not waive the defense of sovereign immunity for the remaining Petitioners who did not file proofs of claim. Pet. Br. at 30 n.36. This argument, however, is unsound. Just as an agency's waiver of sovereign immunity binds the State, it must necessarily also bind the State's other agencies that act on the State's behalf.

The selective waiver of sovereign immunity that Petitioners advocate conflicts with the very nature of sovereignty. Sovereignty flows from the State, not its agencies, and state agencies have sovereign immunity only because they are "arms of the State." The waiver at issue in this case is the waiver of Virginia's immunity because, apart from the State, Petitioners have no immunity. When VMI and other state educational institutions filed proofs of claim, they waived the only immunity that exists: Virginia's immunity. Because the waiver of immunity is Virginia's immunity, there is no immunity left for Central, New River, and Blue Ridge to assert even though these agencies did not file proofs of claim. In any event, wholly apart from the filing of claims, *each* of the Petitioners also participated in the bankruptcy case, and obtained benefits as a result, which in and of itself waived the State's immunity.

The preeminent purpose of sovereign immunity is to accord a *State* the dignity that is consistent with its status as a sovereign. *Federal Mar. Comm'n v. South Carolina State Ports Auth.*, 535 U.S. 743, 760 (2002). When deciding whether a state agency may invoke a State's sovereign immunity, courts routinely inquire into the relationship between the agency and the State, with the relevant inquiry being whether the agency is properly "an arm of the State." *See Regents of the Univ. of Cal. v. Doe*, 519 U.S. 425, 430 (1997). In this case, Petitioners assert unequivocally that they are "the Commonwealth [of Virginia] for purposes of sovereign immunity." Pet. Br. at 1 n.1. In conformity with that contention, Petitioners cannot be considered four separate and distinct sovereigns. Neither sovereign immunity nor the dignity that it is designed to safeguard can be partitioned into portions for each of Virginia's agencies independently to reserve or waive *ad hoc* as their individual or coordinated strategic litigation interests may dictate.

The Second Circuit's decision in *In re Charter Oak Assocs.*, 361 F.3d 760 (2d Cir. 2004), *cert. denied*, 125 S. Ct. 408 (2004), illustrates this principle. In *Charter Oak*, a Connecticut agency filed a proof of claim on behalf of the State against the debtor's bankruptcy estate. 361 F.3d at 763. When the bankruptcy trustee later brought an action against the State asserting the liability of a different Connecticut agency to the estate, the State argued that the filing of the proof of claim by one agency waived sovereign immunity only for that agency. *Id.* at 763-64. Citing *Lapides*, the Second Circuit held that "the fundamental driving force behind the waiver-by-litigation doctrine . . . demands that a waiver by one [agency] be deemed to extend to the other." *Id.* at 772.

A compelling reason for the rule that an agency's waiver binds the State is to prevent the selective use of immunity to achieve unfair litigation advantage. Obviously, if the particular agency that filed a proof of claim is deemed to have waived the State's sovereign immunity, but the State's other agencies are not bound by this waiver, a State could engage in endless

manipulation of its immunity. For example, the State could assign to one of its agencies the task of collecting claims in bankruptcy and participating in the bankruptcy process on behalf of the State, and assign to other agencies the task of collecting and receiving payments outside of bankruptcy. Inevitably, States would quickly become dimorphous super-creditors with the ability to obtain the full benefits of bankruptcy law without having to bear any of its burdens – all at the expense of other creditors and the central bankruptcy policy of equality of distribution. Such a selective subdivision of the State's sovereign immunity, however, is the very result that this Court rejected in *Lapides*, 535 U.S. at 620.

Virginia cannot have it both ways. Having sought and obtained the benefits of the bankruptcy process, Virginia as a whole must abide the consequences. If Virginia does not wish to be bound by ordinary bankruptcy procedures attendant to the filing of proofs of claim, then Virginia should direct its agencies to refrain from filing claims.

4. A state agency's waiver of sovereign immunity by filing a proof of claim includes waiver of sovereign immunity with respect to any preference action that the estate may have against the State or its agencies.

Petitioners' argue that any waiver of Virginia's sovereign immunity is limited to consideration of the specific claims presented in the proofs of claim, to certain compulsory counterclaims, or is capped by the amounts asserted in the claims. Pet. Br. at 22. These contentions are also without merit. Sovereign immunity is a defense to a federal court's *jurisdiction*, and not a defense to a particular claim or categories of claims. Where a State voluntarily invokes the jurisdiction of a federal court by filing a proof of claim, the form of relief sought by or against the State is not relevant to the question whether the State's sovereign immunity has been waived. *Lapides*, 535 U.S. at 620 (citing *Clark*, 108 U.S. at 477; *Gardner*, 329 U.S. at 574;

and *Gunter*, 200 U.S. at 284); *see also Regents of the Univ. of Cal.*, 519 U.S. at 430. A bankruptcy court has plain jurisdiction to allow or disallow claims, and to adjudicate counterclaims against those who have filed proofs of claim, including preference actions. 28 U.S.C. §§ 157(b)(1), 157(b)(2)(B), 157(b)(2)(C), 157(b)(2)(F). The filing of the proofs of claim in this case triggered this jurisdiction.

In addition, the preference actions are necessarily related to the claims. Petitioners' preference obligations to the estate under sections 547, 551, 542, and 550 of the Code arise because they have received transfers of property (funds) that enabled them to recover more on their claims than bankruptcy law allows. By force of section 502(d), any claims that Petitioners hold must be disallowed because of the preferences that they have received. Accordingly, in order to determine whether the claims must be allowed or disallowed, the bankruptcy court must determine whether Petitioners received preferences under section 547. In other words, the preference proceedings that Respondent initiated in this case are intimately connected with the determination of Petitioners' claims because, under applicable bankruptcy law, it is not possible to allow the claims without determining the preferences.

By operation of law, if Petitioners received avoidable preferences, they are not entitled to keep them because section 551 preserves any avoided transfer for the benefit of the estate, and section 542 directs that the avoided transfer must be returned to the estate. Once having determined that Petitioners received preferences, it follows that the bankruptcy court may direct that the funds be returned to the estate under section 550, all as a consequence of the resolution of filed claims.

As this Court has explained in considering the effect of a creditor's filing of a proof of claim on a bankruptcy court's ability to determine a preference action against the creditor, a filed proof of claim "becomes part of the claims-allowance process" that is "integral to the restructuring of the debtor-

creditor relationship through the bankruptcy court's equity jurisdiction." *Langenkamp v. Culp*, 498 U.S. 42, 45 (1990). Accordingly, the filing of a claim triggers not merely the determination of the claim, but the overall equitable process of the "allowance and disallowance of claims," and waives the creditor's Seventh Amendment right to a jury trial with respect to any subsequent preference claim brought by the estate. *Granfinanciera, S.A. v. Nordberg*, 492 U.S. 33, 58-59 & n.14 (1989) (citing *Katchen v. Landy*, 382 U.S. 323, 336 (1966)). By analogy, just as a creditor waives its personal right to a trial by jury in a preference action when the creditor files a proof of claim, a state agency that has filed a proof of claim waives the State's sovereign immunity when the bankruptcy estate asserts that the State must return the preferences that it received.

In *Alexander v. Hillman*, 296 U.S. 222 (1935), the Court held that a federal district court in a receivership proceeding had jurisdiction to adjudicate claims for affirmative relief against parties who filed claims in the proceeding. 296 U.S. at 238. After the creditors in *Alexander* asserted their claims, the district court granted the receivers leave to file an ancillary bill to recover from the claimants certain sums that they allegedly owed to the receivership estate. *Id.* at 236. The claimants defended on the basis that they were not subject to the jurisdiction of the district court because they were citizens of a different State. *Id.* On appeal, this Court expressly rejected the contention that the claimants could invoke the district court's jurisdiction to obtain payment on their claims while denying the court's power to require them to account for what they owed to the estate. *Id.* at 241. In support of its holding, the Court relied upon the interconnected nature of the parties' claims and counterclaims, as well as upon notions of fundamental fairness and judicial economy. *Id.* at 242-43. The Court also overturned the limit that the lower court had placed on the receivers' ability to seek enforcement of only "so much of their claims as are 'purely defensive,'" and held that the district court had jurisdiction over the claimants with regard to the full amount of the receivers' claims for affirmative relief. *Id.*

Similarly, in *Clark v. Barnard*, 108 U.S. 436 (1883), the Court dealt with Rhode Island's claim of sovereign immunity in a context in which Rhode Island made a claim against a fund in federal court. The Court held that the State's appearance in federal court to claim the fund constituted a voluntary submission to federal jurisdiction "to the full extent required for [the] complete determination" of the dispute between the parties. 108 U.S. at 447-48.

As in both *Alexander* and *Clark*, the full determination of Virginia's legitimate interests in the bankruptcy estate in this case requires not only consideration of the various proofs of claim, but also the adjudication of the estate's preference claims. As a result of the invocation of the bankruptcy court's jurisdiction over the former, Petitioners must accept the consequence that they are amenable to the latter.[15]

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[15] In support of their argument that Virginia's waiver of sovereign immunity is limited only to the amount and kind of relief requested in the proofs of claim, Petitioners cite three of this Court's decisions: *United States v. United States Fid. & Guar. Co.*, 309 U.S. 506 (1940); *United States v. Shaw*, 309 U.S. 495 (1940); and *Oklahoma Tax Comm'n v. Citizen Band Potawatomi Tribe*, 498 U.S. 505 (1991). Pet. Br. at 22 & n.25. As this Court pointed out in *Lapides*, however, these three cases are inapposite to the issue as they did not involve the Eleventh Amendment but concerned special circumstances relating to the United States' sovereign interests which were not at issue in that case and, likewise, are not at issue here. *Lapides*, 535 U.S. at 623.

B. Petitioners Cannot Invoke Sovercign Immunity Because the Adversary Proceedings Were Brought By the Court-Appointed Representative of A Federally Created Entity That Falls Under the Supervision of the Department of Justice.

1. The Court should consider Respondent's "federal entity" argument.

If it has not been waived, the defense of sovereign immunity is nonetheless unavailable to Petitioners because the plaintiff in the adversary proceedings at issue is the court-appointed representative of a federally created bankruptcy estate asserting federal claims arising under the federal Bankruptcy Code under the supervision of the Department of Justice.

Petitioners may contend that Respondent is precluded from asserting this argument on the ground that it was not raised or addressed below. This contention, however, is erroneous and the Court should consider Respondent's argument for three reasons. First, Respondent argued below that Petitioners have no defense of sovereign immunity due to the special nature of bankruptcy proceedings, and Respondent's "special entity" argument is not a separate claim, but simply an argument in support of his claim. *See Harris Trust & Sav. Bank v. Salomon Smith Barney, Inc.*, 530 U.S. 238, 245 n.2 (2000) ("'Once a federal claim is properly presented, a party can make any argument in support of that claim; parties are not limited to the precise arguments they made below.'") (quoting *Yee v. Excondido*, 530 U.S. 519, 534 (1992)); *Lebron v. National R.R. Passenger Corp.*, 513 U.S. 374, 379 (1995) (holding that party may present "new argument to support what has been his consistent claim").

Second, the issue is "subsidiary" to the ultimate question of the constitutionality of section 106 because the issue is an integral part of the analysis and is essential to its intelligent resolution. *See Caterpillar, Inc. v. Lewis*, 519 U.S. 61, 75 n.13

(1996) (where resolution of issue is a "predicate to an intelligent resolution of the question presented . . . [it is properly] one 'fairly included' within the question presented"); *Missouri v. Jenkins*, 515 U.S. 70, 84 (1995) (issue "subsidiary to the ultimate inquiry" is "fairly included in the question presented") (internal quotation marks and citation omitted); *Caspari v. Bohlen*, 510 U.S. 383, 389 (1994); *see also Procunier v. Navarette*, 434 U.S. 555, 559 (1978) ("our power to decide is not limited by the precise terms of the question presented"). Section 106 cannot be unconstitutional if it authorizes nothing more than what the Eleventh Amendment permits. If the Eleventh Amendment permits the representative of a bankruptcy estate to pursue preference actions against Petitioners, then Petitioners' claim of unconstitutionality must fail. Because only trustees may pursue preference actions, the issue is integral to the question.

Third, the question of sovereign immunity is one of jurisdiction and questions of jurisdiction may be raised at any time, *See FW/PBS, Inc. v. City of Dallas*, 493 U.S. 215, 230-31 (1990) (considering standing issue not raised or addressed below that implicated federal jurisdiction because "every federal appellate court has a special obligation to satisfy itself not only of its own jurisdiction, but also that of the lower courts in a cause under review.") (internal quotation marks and citation omitted).

2. The bankruptcy estate is a special entity to which the Eleventh Amendment does not apply.

The Eleventh Amendment provides that "the judicial power of the United States shall not be construed to extend to any suit in law or equity, commenced or prosecuted against one of the United States by Citizens of another State, or by Citizens or Subjects of any Foreign State." U.S. Const. amend. XI. Although, by its literal terms, the amendment "restrict[s] only the Article III diversity jurisdiction of the federal courts," *Seminole Tribe*, 517 U.S. at 54, the Court has concluded that the text of the amendment is not controlling. Instead, the amendment reflects broader principles of sovereign immunity, *Alden v.*

Maine, 527 U.S. 706, 715-17 (1999). Thus, the Court has held that the amendment shields States from suits by their own private citizens, *Hans v. Louisiana*, 134 U.S. 1 (1890); by foreign countries, *Principality of Monaco v. Mississippi*, 292 U.S. 313 (1934); and by Indian tribes, *Blatchford v. Native Village of Noatak*, 501 U.S. 775 (1991).

On the other hand, "nothing in [the Eleventh Amendment] or any other provision of the Constitution prevents or has ever been seriously supposed to prevent a State's being sued by the United States." *United States v. Mississippi*, 380 U.S. 128, 140-141 (1965). The same is true for suits between States. As the Court recently observed, the Constitution contemplates suits "among the members of the federal system as an alternative to extralegal measures." *Alden*, 527 U.S. at 755-756.

This Court first addressed whether the United States may sue a State in *United States v. Texas*, 143 U.S. 621 (1892), a dispute over the ownership of real property claimed by both sovereigns. Congress, by statute, had directed the Attorney General to commence suit on behalf of the United States "in order that the rightful title to said land may be finally determined." 143 U.S. at 622. Texas claimed that the federal government lacked constitutional authority to sue a State in federal court. This Court, however, was unwilling to assume that the Constitution "overlooked the possibility that controversies, capable of judicial solution, might arise between the United States and some of the States," particularly where the Constitution makes other inter-sovereign controversies cognizable in federal court. *Id.* at 644-45. Acknowledging the federal jurisdictional limits represented by the Eleventh Amendment, the Court nevertheless interpreted the Constitution as inherently subjecting the States to "the suit of the government established for the common and equal benefit of the people of all the States." *Id.* at 646.

This case presents a close variant on the well-settled principle that States cannot claim sovereign immunity as a

defense to an action brought by or on behalf of the federal government. Here, Respondent is the court-appointed official responsible for representing the real party in interest – the federally created bankruptcy estate that resides *in custodia legis* with the federal bankruptcy court. The bankruptcy estate is obviously not a private citizen. Nor is it a citizen of any State. Rather, it is a creature of federal law that resides exclusively in the custody of the United States.

Nor is a bankruptcy trustee a private litigant, but, rather, is an official of the United States. In the performance of his or her duties, a bankruptcy trustee acts as an agent of the bankruptcy court. *See* 11 U.S.C. §§ 323, 324, 327, 330, 1104; *see also River Prod. Co. v. Webb (Matter of Topco, Inc.)*, 894 F.2d 727 (5th Cir. 1990). Further, bankruptcy trustees are subject to the considerable supervision of the United States Trustee, who is a Department of Justice official and who is also authorized to serve as a trustee in bankruptcy cases. *See* 28 U.S.C. § 586; *Balser v. Department of Justice*, 327 F.3d 903, 910 (9th Cir. 2003); *Joelson v. United States*, 86 F.3d 1413, 1418 (6th Cir. 1996). By virtue of their office as agents of the federal court, bankruptcy trustees enjoy qualified immunity from suit similar to other governmental officials,[16] and, in at least one respect, enjoy one type of protection from suit greater than that of most other federal officers.[17]

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[16] *See, e.g., Curry v. Castillo (In re Castillo)*, 297 F.3d 940, 949-52 (9th Cir. 2002), *amended by*, Nos. 00-55846, 00-55851, 2002 U.S. App. LEXIS 25729 (9th Cir. Sept. 6, 2002), (discussing bankruptcy trustee's immunity from suit); *Gregory v. United States Bankr. Court*, 942 F.2d 1498, 1500-01 (10th Cir. 1991) (holding trustee entitled to absolute immunity with respect to certain official functions).

[17] *See, e.g., In re Linton*, 136 F.3d 544, 546 (7th Cir. 1998); *Lebovits v. Scheffel (In re Lehal Realty Assocs.)*, 101 F.3d 272 (2d Cir. 1996); *Allard v. Weitzman (In re DeLorean Motor Co.)*, 991 F.2d 1236, 1240 (6th Cir. 1993); *Vass v. Conron Bros. Co.*, 59 F.2d 969, 970 (2d Cir.

Apart from his duties to the estate and to the bankruptcy court, Respondent has no individual stake in the outcome of this case.[18] Rather, the preference proceedings at issue were instituted on behalf of the estate for the collective benefit of creditors, including various other governmental entities. Although the estate in this case is obviously not the United States itself, it is also not a private citizen, a citizen of any State, or a citizen of a foreign State. As a federally created instrumentality of the United States, the bankruptcy estate should enjoy the same privilege of suit as the United States with respect to federal causes of actions arising under the Bankruptcy Code that are necessary to fulfill the critical functions of the Code.

The Court's decisions in *Blatchford* and *Alden* are not to the contrary. Both involved suits by private individuals seeking to enforce their own personal rights. In contrast, this case involves the pursuit of a federally created cause of action by an instrumentality of the United States. Neither *Blatchford* nor *Alden* addresses this situation. On the contrary, *Blatchford* belongs to the category of cases in which the Court has required proof that a federal sovereign interest, or federal quasi-sovereign interest, is actually at stake when a suit appears to benefit only private persons. 501 U.S. at 779-87. That concern has no relevance here. The preference proceedings were instituted to benefit the estate, a federal entity, in order to fulfill the federal policies of the Bankruptcy Code.

1932). In each of these cases, the court applied the rule referred to as the "Barton doctrine." The Court in *Barton v. Barbour*, 104 U.S. 126, 127 (1881), stated that "[i]t is a general rule that before suit is brought against a receiver[,] leave of the court by which he was appointed must be obtained."

[18] Disinterest is a requirement for appointment as a bankruptcy trustee. 11 U.S.C. § 1104(b); *see also Wolf v. Weinstein*, 372 U.S. 633, 651 (1963).

The Court's decision in *Smith v. Reeves*, 178 U.S. 436 (1900), is also not to the contrary. *Smith* involved the federal court receivership of the Atlantic and Pacific Railroad Company, a federally chartered corporation. 178 U.S. at 436-37. The receiver commenced a suit against the treasurer of California under a *state* statute permitting the recovery in state court of taxes improperly collected by the State. *Id.* at 437. The Court concluded that the receiver was required to pursue the action in state court, rather than in federal court, on the ground that the State had only consented to be sued in its own court. *Id.* at 441. This case presents a different issue not addressed in *Smith*: whether a trustee acting on behalf of a federally created bankruptcy estate may enforce an action arising under *federal* law for which the trustee has no alternative state court forum or remedy. *Compare Osborn v. Bank of the United States*, 22 U.S. (9 Wheat.) 738 (1824) (holding federal jurisdiction appropriate notwithstanding Eleventh Amendment in federally chartered bank's suit against treasurer of Ohio where rights asserted were founded on integral parts of federal law that created bank).

The Court has recognized that the Eleventh Amendment is not a bar to suits by the United States seeking to enforce or protect governmental, or quasi-governmental interests. For example, notwithstanding the Eleventh Amendment, the federal government may sue a State in federal court, or one State may sue another in federal court, for relief that benefits private parties provided the litigation also serves larger sovereign goals. *See North Dakota v. Minnesota*, 263 U.S. 365, 375-76 (1923) (holding that one State can sue another "to protect the general comfort, health or property rights of its inhabitants"). So long as "sovereign or quasi-sovereign interests are implicated," and the sovereign "is not merely litigating as a volunteer the personal claims of its citizens," the Eleventh Amendment does not bar the claim. *Pennsylvania v. New Jersey*, 426 U.S. 660, 665 (1976) (*per curiam*); *see also Alfred L. Snapp & Son, Inc. v. Puerto Rico*, 458 U.S. 592, 600-01 (1982). Although "neither an exhaustive formal definition nor a definitive list of qualifying interests can be presented in the abstract," the Court has focused

on such considerations as the subject matter of the suit (e.g. the general well-being of the sovereign's citizenry), the sovereign's ability "to address [the asserted injury] through its [own] sovereign lawmaking powers," and the sovereign's interest "in assuring that the benefits of the federal system are not denied to its general population." *Snapp*, 458 U.S. at 607-608.

Similar sovereign and quasi-sovereign interests of the United States are at work when a bankruptcy trustee pursues a federal preference proceeding. In particular, the trustee seeks to promote equality of distribution among all creditors (including governmental creditors), and discourage debt collection activities against debtors struggling on the verge of bankruptcy. Congress has chosen a judicial officer of the bankruptcy court supervised by an official of the Department of Justice to fulfill these policies for the benefit of the federally created bankruptcy estate and the public interest. Accordingly, the matter is a close variant of a suit by the United States and the Court should conclude that the Eleventh Amendment poses no bar to its pursuit in this case.

C. Sovereign Immunity Is Not Available to Bar the Bankruptcy Court's *In Rem* Jurisdiction Over Property that Should Be Returned to the Bankruptcy Estate.

1. The Court should consider Respondent's *in rem* argument.

This Court has long recognized that state and federal officials may not retain property, including funds, that they have no right to keep under federal law. Under the Fifth and Fourteenth Amendments, this Court has not hesitated to require monetary relief for the retention of property taken without just compensation, and clearly the Eleventh Amendment poses no bar to such a remedy. Separate and apart from this jurisprudence, the Court has also long recognized the *in rem* rule that a federal court may direct the relinquishment of property (including funds) that a federal or state agency has no right to

retain under federal law. In this case, Respondent seeks *in rem* to recover property (funds) that Petitioners have received but have no right to keep under federal bankruptcy law. Bankruptcy courts must possess, and be able to exercise, a comprehensive *in rem* authority over property of the kind at issue in this case because if they are denied this power then the essential aims of the Bankruptcy Code would be repeatedly thwarted. For the reasons noted above with respect to Respondent's waiver and federal entity arguments, the Court should consider Respondent's *in rem* argument.

2. Bankruptcy courts possess broad *in rem* authority to marshal the assets of an estate and adjust the rights of creditors.

This Court has observed that bankruptcy proceedings are fundamentally *in rem* in nature, and that, as noted, upon commencing a bankruptcy case, the debtor's property resides fully in the custody of the bankruptcy court. *Straton v. New*, 283 U.S. 318, 320-21 (1931); *Acme Harvester Co. v. Beekman Lumber Co.*, 222 U.S. 300, 306-07 (1911); *see also Hood*, 541 U.S. at 448 (discussing bankruptcy court's *in rem* jurisdiction). The *in rem* nature of bankruptcy proceedings extends to the critical bankruptcy functions of marshalling an insolvent debtor's assets and the adjustment and payment of claims against those assets. *Straton*, 283 U.S. at 320-21 ("The purpose of the Bankruptcy Act . . . is to place the property of the bankrupt, whereever [sic] found, under the control of the court, for equal distribution among the creditors."); *see also Young v. Higbee Co.*, 324 U.S. 204, 210 (1945) ("historically one of the prime purposes of the bankruptcy law has been to bring about a ratable distribution among creditors of a bankrupt's assets").

A bankruptcy court cannot perform its critical functions of marshalling the debtor's assets and ensuring equality of distribution among creditors if individual creditors, including governmental units, are free to "opt out" of the process, ignore the substantive rules of bankruptcy law, and evade the exclusive

jurisdiction of the bankruptcy court. A governmental unit may not assert sovereign immunity to circumvent the exercise of essential bankruptcy jurisdiction because, if it could, there would be little left to that jurisdiction. In bankruptcy, unless all creditors, including "those cloaked in the mantle of sovereign immunity," are subject to the jurisdiction of the bankruptcy court, bankruptcy's collective mechanism for resolution simply could not operate. *See Irving Trust Co.*, 288 U.S. at 333.

These principles underlie this Court's analyses in *Irving Trust* and *Whiting Pools*, and the Court's recent analysis in *Hood*. In *Irving Trust* the Court observed that, if a State could avoid the bankruptcy procedures governing the resolution of claims, "estates could not be promptly closed." *Irving Trust*, 288 U.S. at 331. To solve this problem, Congress has the right to require all those interested in the debtor's estate, including governmental units, to appear and assert their claims. *Id.* at 332.

More broadly, in order to secure the efficient administration of bankruptcy estates, Congress has the right to bestow exclusive jurisdiction in a single tribunal over the administration of the estate, and the determination and payment of claims. *Irving Trust*, 288 U.S. at 332. To effectuate this power, it has long been recognized that, when a federal court takes possession of all of the assets of the debtor, that court's jurisdiction over the assets, and all claims to them, is exclusive of all other courts. *Id.* at 332-33. Drawing these principles together, the Court concluded in *Irving Trust*:

> The Federal government possesses supreme power in respect of bankruptcies. If a state desires to participate in the assets of a bankrupt, she must submit to appropriate requirements by the controlling power; otherwise, orderly and expeditious proceedings would be impossible and a fundamental purpose of the Bankruptcy Act would be frustrated.

Id. at 333 (citation omitted).

In *Whiting Pools*, the Court conducted a similar analysis in considering the *in rem* authority of the bankruptcy court over property of the debtor that the IRS had seized immediately prior to the debtor's commencement of its bankruptcy case. The Court observed that, in defining the boundaries of the bankruptcy estate, Congress included within those boundaries not only property in the debtor's possession at the time of the bankruptcy filing, but also "any property made available to the estate by other provisions of the Code." *Whiting Pools*, 462 U.S. at 205. The Court observed that "[s]everal of these provisions bring into the estate property in which the debtor did not have a possessory interest at the time the bankruptcy proceeding commenced" and specifically listed section 547 as an example, noting "[t]hese sections permit the trustee to demand the turnover of property that is in the possession of others if that possession is due to . . . a preferential transfer." *Id.* at 205 & n.10; *see also Begier*, 496 U.S. at 58 ("'property of the debtor' subject to the preferential transfer provision is best understood as that property that would have been part of the estate had it not been transferred before the commencement of bankruptcy proceedings").

As the Court reasoned, unless the estate can recover and make use of the debtor's various interests in property, the essential purposes of bankruptcy would be frustrated. *Whiting Pools*, 462 U.S. at 203 (noting that, without access to the debtor's property, reorganization would not be possible). Accordingly, the Court held that property belonging to the estate, but in the possession of the government, must be turned over for administration in accordance with applicable bankruptcy procedures. *Id.* at 211-12.

In *Hood*, the Court continued this line of analysis in considering the *in rem* authority of the bankruptcy court over the debtor's effort to discharge an obligation owing to a state agency. Citing *Irving Trust*, the Court observed that "States, whether or not they choose to participate in the proceeding, are bound by a bankruptcy court's discharge orders no less than other creditors." *Hood*, 541 U.S. at 448. Similarly, citing *Van*

Huffel v. Harkelrode, 284 U.S. 225, 228-29 (1931) – a case in which the Court approved the bankruptcy court's sale of property free and clear of a State's tax lien – the Court stated that "our cases indicate that the exercise of [a bankruptcy court's] *in rem* jurisdiction to discharge a debt does not infringe state sovereignty." *Hood*, 541 U.S. at 448. Accordingly, the Court affirmed the bankruptcy court's *in rem* determination of the debtor's discharge. *Id.* at 451.

3. The administration of the Code's preference avoidance and recovery rules lies within the bankruptcy court's *in rem* authority and does not constitute a suit for money damages.

A proceeding to avoid and recover a preferential transfer under sections 547, 542, 550, and 551 of the Bankruptcy Code is an *in rem* proceeding to determine the bankruptcy estate's title to property and marshal the property to facilitate the estate's administration. As this Court explained in *Gardner*, the *in rem* jurisdiction of the bankruptcy court over property of the estate "is not limited to the prevention of interference with the use of the property by the trustee; it 'extends also to the adjudication of questions respecting title.'" *Gardner*, 329 U.S. at 577 (quoting *Ex Parte Baldwin*, 291 U.S. 610, 616 (1934) and *Thompson v. Texas Mexican Ry. Co.*, 328 U.S. 134, 140 (1946)). Applying this longstanding rule, the Court concluded in *Gardner* that the bankruptcy court had jurisdiction over property in which the State of New Jersey claimed a superior interest. *Gardner*, 329 U.S. at 578; *see also Straton*, 283 U.S. at 322 (holding bankruptcy court that avoids lien "has jurisdiction to administer the property regardless of the lien"); *Van Huffel*, 284 U.S. at 228 (observing bankruptcy court's obligation to "reduce to money and distribute the estates of bankrupts, *and to determine controversies with relation thereto*") (emphasis added).

Under section 547, the relevant *in rem* inquiry is likewise one of title. By its terms, section 547 operates to avoid the debtor's pre-petition transfer of property, thus defeating the

transferee's title to the property. Specifically, section 547 provides that "the trustee may *avoid* any transfer of an interest of the debtor in property" if the criteria of section 547 apply. 11 U.S.C. § 547 (emphasis added). Application of section 547 is little different than the avoidance of a State's lien on the debtor's property at issue in *Van Huffel* or *Straton*: each involves simply a determination of the State's interest in property that may be administered as part of the bankruptcy estate.

Under sections 542, 550, and 551, the relevant *in rem* procedure involves marshalling property that belongs to the estate and that may be administered as part of the estate. To begin with, section 551 provides that, if a transfer is avoided under section 547, the transfer is automatically preserved for the benefit of the estate. 11 U.S.C. § 551 ("Any transfer avoided under section . . . 547 . . . *is preserved for the benefit of the estate*.") (emphasis added). In other words, once a transfer is avoided, title to the *res* vests automatically in the estate.

In turn, section 542 directs that anyone in possession of property of the estate must turn over the property to the trustee. 11 U.S.C. § 542(a) ("[A]n entity . . . in possession, custody, or control . . . of property that the trustee may use, sell, or lease . . . shall deliver to the trustee . . . *such property*." (emphasis added). Likewise, section 550 authorizes the bankruptcy court to require the transferee of an avoided transfer to relinquish the property to the estate. 11 U.S.C. § 550(a) ("to the extent that a transfer is avoided under section . . . 547 . . . the trustee may recover, for the benefit of the estate, *the property transferred*") (emphasis added). Application of these provisions is little different than the procedure recognized in *Whiting Pools* that a governmental agency is obligated under section 542 to return property that it had seized to the estate on account of a tax claim.

In this case, of course, the property in question is specific funds that Wallace transferred to Petitioners. The fact that the property is funds, however, does not defeat the *in rem* nature of the proceedings nor does it convert the matter into a suit for

money damages. The nature of the relief requested is controlling. Here Respondent seeks the recovery of the property that was transferred, which happens to be funds, not damages for wrongful retention of the property. This Court has previously approved this very distinction in *Bowen v. Massachusetts*, 487 U.S. 879, 893-96 (1988). There the Court observed that "[t]he fact that a judicial remedy may require one party to pay money to another is not a sufficient reason to characterize the relief as 'money damages.'" 487 U.S. at 893. The Court explained that "[d]amages are given to the plaintiff to *substitute* for a suffered loss, whereas specific remedies are not substitute remedies at all, but attempt to give the plaintiff the very thing to which he was entitled." *Id.* at 895 (internal quotation marks and citation omitted); *see also Aetna Cas. & Sur. Co. v. United States*, 71 F.3d 475, 478 (2d Cir. 1995) ("[Plaintiff's suit to recover funds] is not for damages to compensate for the government's failure to perform a duty. . . . Rather it seeks to require the government to perform its duty – that is, to pay Aetna funds held by the government . . . ."). By its terms, the remedy that section 550 offers and that is at issue here is the specific recovery of property.[19]

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[19] Respondent's complaints in this case request both recovery of the property transferred and recovery of the value of the property transferred. J.A. 9, 16, 26, and 34; *see* 11 U.S.C. § 550(a) (allowing the recovery of the property transferred, or, with court authorization, "the value of such property"). In the event Petitioners have waived sovereign immunity, or Respondent's pursuit of relief is not barred by the Eleventh Amendment for reasons other than Respondent's *in rem* argument, Respondent is entitled to either form of relief. To the extent that the Court determines that the exercise of *in rem* jurisdiction in bankruptcy permits only the recovery of the particular property in question under the Eleventh Amendment, Respondent would amend and limit his complaints to seek only the property transferred.

4. The bankruptcy court may recover a preferential transfer from a State in the exercise of its *in rem* authority, and the Eleventh Amendment does not apply.

A bankruptcy court has no authority to surrender its *in rem* jurisdiction over the administration of the estate. *See Isaacs v. Hobbs Tie & Timber Co.*, 282 U.S. 734, 739 (1931) ("[A] court of bankruptcy itself is powerless to surrender its control of the administration of the estate."). Likewise, State officials have no authority – and, critically, no defense of sovereign immunity – to refuse the superior claim of the bankruptcy estate to property that can be administered as part of the federal bankruptcy proceeding. Certainly Petitioners had the right to collect debts from Wallace before Wallace filed for bankruptcy. But state law debt-collection procedures, and the rights that they bestow, must yield to the requirements of the governing Bankruptcy Code. *See Perez v. Campbell*, 402 U.S. 637, 649 (1971) (invalidating under the Supremacy Clause a state statute enforced by a state agency that provided for the recovery of tort claims in violation of the Bankruptcy Act's discharge provisions); *Van Huffel*, 284 U.S. at 228 (holding that realization on state tax lien "must yield" to the requirements of bankruptcy law); *see also International Shoe Co. v. Pinkus*, 278 U.S. 261, 265 (1929); *Cohens v. Virginia*, 19 U.S. 264, 414 (1821).

It cannot be otherwise. Governmental units, particularly state tax authorities, are pervasive creditors in bankruptcy proceedings. If governmental agents need not return preferential payments to the bankruptcy estate, then the fundamental aims of bankruptcy law would be thwarted. *See Hoffman v. Connecticut Dep't of Income Maint.*, 492 U.S. 96, 110 (1989) (Marshall, J., dissenting) ("[If the States need not adhere to the preference rules,] any State owed money by a debtor with financial problems will have a strong incentive to collect whatever it can, as fast as it can, even if doing so pushes the debtor into bankruptcy. Ordinary creditors will soon realize that State can

receive more than their fair share; the very existence of this governmental power will cause these other creditors, in turn, to increase pressure on the debtor."). Accordingly, just as state officials must abide other bankruptcy procedures, they must likewise abide the preference rules.

This Court has long recognized an exception to the doctrine of sovereign immunity for actions to recover property (including money) in the hands of a State official where, under applicable federal law, the State or its agent has no lawful right to retain possession. Under this exception, the Court has recognized the right of a federal court to determine not only questions of title, but also decree surrender of the property.

For example, in *Osborn v. Bank of the United States*, 22 U.S. 738 (1824), the Court approved an action brought by a federally chartered bank to recover funds wrongfully seized by officials of the State of Ohio. In concluding that the action could proceed, the Court explained: "It was proper, then, to make a decree against the defendants in the Circuit Court, if the law of the State of Ohio [directing the seizure of the bank's property] be repugnant to the constitution, or to a law of the United States made in pursuance thereof, so as to furnish no authority to those who took, or to those who received, the money for which this suit was instituted." 22 U.S. at 859; *see also United States v. Peters*, 9 U.S. 115, 139-40 (1809) (directing the return of property to its rightful owner and stating that "it certainly can never be alleged, that a mere suggestion of title in a state to property, in possession of an individual, must arrest the proceedings of the court, and prevent their looking into the suggestion, and examining the validity of the title").

Similarly, in *United States v. State Bank*, 96 U.S. 30 (1877), the United States came into possession of $480,000 in currency belonging to a bank owing to the misconduct of one of the federal government's treasury officers. The funds were transferred to the federal Treasury in Washington. In affirming the decision of the court of claims requiring that the funds be

returned to their rightful owner, the Court explained that the right of possession by the United States could be avoided: "[The] doings [of the treasury officer as agent for the United States in receiving the funds] were vitiated by the underlying dishonesty, and could confer no rights upon [the United States]." 96 U.S. at 36; *see Bull v. United States*, 295 U.S. 247, 261 (1935) (clarifying that the exception to immunity discussed in the *State Bank* case does not turn on the participation of the sovereign in any fraud or deceit); *see also Land v. Dollar*, 330 U.S. 731, 738 (1947) (holding that private individuals could maintain an action against officials of the United States Maritime Commission for stock that the officials were alleged to have wrongfully retained; stating "[a]nd where they unlawfully seize or hold a citizen's realty or chattels, recoverable by appropriate action at law or in equity, [the private citizen] is not relegated to the Court of Claims to recover a money judgment"); *Sante Fe Pac. R.R. Co. v. Payne*, 259 U.S. 197, 198-200 (1922); *Ex Parte Young*, 209 U.S. 123, 158 (1908); *Smith v. Reeves*, 178 U.S. 436, 439 (1900) ("[T]he settled doctrine of this court is that the question of possession does not cease to be a judicial question – as between the parties actually before the court – because the defendant asserts or suggests that the right of possession is in the state of which he is an officer or agent."); *Tindal v. Wesley*, 167 U.S. 204, 221 (1897) (upholding property owner's recovery and stating that "the eleventh amendment gives no immunity to officers or agents of a state in withholding the property of a citizen without authority of law"); *Noble v. Union River Logging R.R. Co.*, 147 U.S. 165, 172, 176 (1893); *United States v. Lee*, 106 U.S. 196, 219-20 (1882); *Meigs v. M'Clung's Lessee*, 13 U.S. 11, 18 (1815).

In *Florida v. Treasure Salvors, Inc.*, 458 U.S. 670 (1982) (plurality), a party claiming rights to the shipwreck *Atocha* commenced an *in rem* admiralty proceeding regarding the wreck. Prior to the proceeding, certain artifacts from the wreck had been transferred to an agency of the State of Florida. The district court ordered the items turned over to the custody of the court. This Court affirmed, concluding that "[t]he Eleventh

Amendment . . . did not bar the process issued by the District Court to secure possession of the artifacts of the *Atocha* held by the named state officials." 458 U.S. at 699.

More recently, in *California v. Deep Sea Research, Inc.*, 523 U.S. 491 (1998), the Court reviewed extensively its decision in *Treasure Salvors* and considered whether a federal court sitting in admiralty could determine the claim of a State without its consent to property (the shipwreck *Brother Jonathan*) in the custody of the court. Citing *Tindal* and other precedents that permitted the determination of title to property over which the federal court exercises *in rem* authority, the Court concluded that a federal court in the exercise of its *in rem* admiralty jurisdiction may determine the interests of the various parties, including the State: "[W]e conclude that the Eleventh Amendment does not bar federal jurisdiction over the *Brother Jonathan* and, therefore, that the District Court may adjudicate DSR's and the State's claims to the shipwreck." 523 U.S. at 507-08.

Read together, *Treasure Salvors* and *Deep Sea* reaffirm the principles established in such cases as *State Bank*, *Bull*, *Lee*, *Noble*, *Tindal*, *Osborn*, *Land*, and *Sante Fe* that a federal court applying federal law (1) may require the turnover of property from a State agency in cases in which the agency's retention of the property is in violation of federal law; and (2) may adjudicate all interests in the property in the exercise of its *in rem* jurisdiction over the property in question. These principles apply with equal force in bankruptcy.

Citing *Deep Sea*, this Court observed in *Hood* that, notwithstanding the Eleventh Amendment, "States . . . may still be bound by some judicial actions without their consent." *Hood*, 541 U.S. at 446. Observing further that "[b]ankruptcy courts have exclusive jurisdiction over a debtor's property, wherever located, and over the estate," *id.* at 447, the Court determined that "[a] bankruptcy court's *in rem* jurisdiction permits it 'to determin[e] all claims that anyone, whether named in the action or not, has to the property or thing in question,'" *id.* at 448

(quoting 16 James Wm. Moore, et al., MOORE'S FEDERAL PRACTICE § 108.70[1], p. 108-106 (3d ed. 2004)). Once again citing *Deep Sea*, the Court stated: "Although both bankruptcy and admiralty are specialized areas of the law, we see no reason why the exercise of the federal courts' *in rem* bankruptcy jurisdiction is more threatening to state sovereignty than the exercise of their *in rem* admiralty jurisdiction." *Hood*, 541 U.S. at 451.

In this case, Respondent seeks from Petitioners recovery of property that Wallace transferred to them. In exchange, Petitioners are entitled to assert claims against the bankruptcy estate for the preferences that they return, and may receive distributions from the estate on account of their claims. *See* Fed. R. Bankr. P. 3002(c)(3). The fact that Petitioners are denied the benefit of certain property that they are not entitled to retain does not violate the Eleventh Amendment.

The Court's decision in *United States v. Nordic Village, Inc.*, 503 U.S. 30 (1992) is not to the contrary. In *Nordic Village*, the Court considered the question whether the predecessor statute to current section 106 of the Bankruptcy Code established an unequivocal textual waiver of the sovereign immunity of the United States with respect to a trustee's pursuit of a transfer made to the IRS. 503 U.S. at 31. Concluding that it did not, the Court then considered the argument whether the trustee's pursuit of a claim for *money damages* could be sustained under the bankruptcy court's *in rem* jurisdiction. *Id.* at 38. Observing that the trustee sought to recover "a sum of money, not 'particular dollars,'" the Court stated that the premise for an *in rem* argument was missing because the trustee's claim did not focus on any "*res*." *Id.* (citations omitted). In the present case, the argument is focused quite differently. Respondent invokes the *in rem* jurisdiction of the bankruptcy court to recover under section 550 "the property transferred." 11 U.S.C. § 550(a). This Court has approved the recovery of funds from state officials on an *in rem* basis, and the relief that

Respondent seeks in this case is not barred by principles of sovereign immunity.[20]

Moreover, an order requiring state officials to perform some duty does not violate principles of sovereign immunity simply because the State may incur some expense arising from compliance with a federal court order. *See Edelman v. Jordan*, 415 U.S. 651, 668 (1974); *see also Missouri v. Jenkins*, 491 U.S. 274, 290 (1989) (O'Connor, J.) (concurring in part with award of attorneys' fees against State and stating that "[t]he Eleventh Amendment does not, of course, provide a State with across-the-board immunity from all monetary relief. Relief that 'serves directly to bring an end to a violation of federal law is not barred by the Eleventh Amendment even though accompanied by a substantial ancillary effect' on a State's treasury") (quoting *Papasan v. Allain*, 478 U.S. 265, 278 (1986)). In this case, Respondent's request for *in rem* relief in the form of requiring turnover of funds that Petitioners received but cannot retain is of the same character and is a type of permissible monetary relief.

5. Respondent is entitled to recover the relevant funds from Petitioners even if Petitioners have disbursed funds from their accounts.

The fact that Petitioners may have disbursed funds from their respective accounts does not prevent Respondent from recovering the funds in question. In circumstances such as these, the law deems that, where money belonging to one entity is transferred to a second entity who must return it, and the second entity disburses the money from its account, the second entity is

[20] As the Court also explained in *Hood*, the fact that the bankruptcy court makes use of a summons and complaint to administer its *in rem* jurisdiction is not controlling. 541 U.S. at 453 ("Thus, whether an *in rem* adjudication in a bankruptcy court is similar to civil litigation in a district court is irrelevant."). What matters is the nature of the proceeding. *Id.* at 453-54.

considered to have expended its own money rather than the money of the rightful owner and the rightful owner's money is still considered to be held by the disbursing party. *See, e.g., Aetna Cas. & Sur. Co.*, 71 F.3d at 479 ("if an agency has a legal obligation to pay money to a party, that duty does not disappear simply because the money was paid in error to the wrong person."). In any event, to the extent that there is any question regarding the adequacy of Respondent's *in rem* remedy in this case, this may be considered upon remand.

D. By Constitutional Design, the States Have No Sovereign Immunity to a Bankruptcy Court's *In Rem* Bankruptcy Jurisdiction.

Congress's authority to enact bankruptcy legislation is set forth in the Bankruptcy Clause as follows: "The Congress shall have Power . . . To establish . . . uniform Laws on the subject of Bankruptcies throughout the United States." U.S. CONST., art. I, § 8, cl. 4 (the "Bankruptcy Power"). Pursuant to its Bankruptcy Power, Congress has provided for the abrogation of a State's sovereign immunity in section 106(a) of the Bankruptcy Code in the application of sections 547, 542, 551, and 550. 11 U.S.C. § 106(a)(1) ("Notwithstanding an assertion of sovereign immunity, sovereign immunity is abrogated as to a governmental unit to the extent set forth in this section with respect to the following: . . . Sections . . . 542, . . . 547, . . . 550, 551."). In *Seminole Tribe*, this Court established a two-prong test to determine whether Congress has validly abrogated a State's sovereign immunity: (1) whether Congress unequivocally expressed its intent to abrogate the sovereign immunity; and (2) whether Congress acted "pursuant to a valid exercise of power." 517 U.S. at 55. Both prongs are satisfied in this case.

1. Congress has unmistakably indicated its intent to abrogate sovereign immunity in the application of sections 547, 542, 550, and 551 under section 106.

In its decision in *Hood*, the Sixth Circuit held that Congress unequivocally expressed its intent to abrogate state sovereign immunity in enacting section 106 of the Code, thereby satisfying the first prong of the *Seminole Tribe* analysis. *Hood*, 319 F.3d at 762. This point is not in dispute.

2. In the exercise of its Bankruptcy Power, Congress has a unique and comprehensive authority that includes the ability to bind States to critical aspects of bankruptcy proceedings – including the preference rules.

The Court has long recognized that the authority to restructure relations between insolvent debtors and their creditors lies at the heart of the federal bankruptcy power. *Northern Pipeline Constr. Co. v. Marathon Pipe Line Co.*, 458 U.S. 50, 71 (1982) (plurality) (the restructuring of debtor/creditor relations lies "at the core of the federal bankruptcy power"). The Court has also long recognized that, as part of the uniformity principle embedded in the Bankruptcy Clause, the scope of the Bankruptcy Power necessarily encompasses a comprehensive authority over the creation of the bankruptcy estate, the marshalling of property of the estate, the determination of title to property that may be included as part of the estate, the recovery of property to be included in the estate, the discharge of the debtor, and the ratable distribution of the estate.

As Chief Justice Marshall wrote for the Court in first discussing the Bankruptcy Clause in *Sturges v. Crowninshield*, 17 U.S. 122 (1819): "The peculiar terms of the grant certainly deserve notice. Congress is not authorized merely to pass laws,

the operation of which shall be uniform, but to establish uniform laws on the subject throughout the United States." 17 U.S. at 193-94. As the Court subsequently explained in *Acme*: "It is the purpose of the bankruptcy law, passed in pursuance of the power of Congress, to establish a uniform system of bankruptcy throughout the United States, to place the property of the bankrupt under the control of the court, wherever it is found, with a view to its equal distribution among the creditors." *Acme*, 222 U.S. at 307; *see also Pinkus*, 278 U.S. at 265 ("The power of Congress to establish uniform laws on the subject of bankruptcies throughout the United States is unrestricted and paramount.").

As Justice Clifford wrote in *Sherman v. Bingham*, 21 F. Cas. 1270 (1st Cir. 1872), a case involving consideration of the jurisdiction of a federal court to direct the recovery of money located outside its territorial jurisdiction to be included as part of the debtor's bankruptcy estate: "Nothing of greater importance is required to be done under and in virtue of the bankruptcy than the collection of the assets belonging to the estate of the bankrupt." *Id.* at 1271. As the court further explained in upholding federal jurisdiction: "Refusal to pay a just debt, is a wrong for which the . . . [bankruptcy trustee] ought to have a remedy not dependent upon the option of a state court, but it is clear that the plaintiff has none such in this case, unless the jurisdiction of the district court in this district is sustained." *Id.* at 1274.

In reaching this conclusion, Justice Clifford observed that the concept of uniformity encompasses a comprehensive authority to deal with the bankruptcy estate and the obligation of any person to transfer property to it: "Comprehensive and explicit as . . . [the Bankruptcy Clause] of the constitution is, it is not possible to doubt that it empowers congress, not only to establish uniform laws on the subject of bankruptcies throughout the United States, but also to commit the execution of the system to such courts of the United States as congress shall see fit, and to prescribe such modes of procedure and means of

administering the system as congress in their discretion shall deem best suited to carry it into successful operation." *Id.* at 1272; *see also id.* at 1273 ("Beyond doubt congress, in enacting the bankrupt law, intended to make it uniform throughout the United States, and in order to secure such uniformity congress obviously intended to create or to designate tribunals and officers to execute all its provisions.").

In *Lathrop v. Drake*, 91 U.S. 516 (1875), the Court expressly adopted Justice Clifford's reasoning in upholding Congress's vesting of the federal courts with a comprehensive federal jurisdiction over the rights and powers conferred under the Bankruptcy Act of 1867:

> [A] uniform system of bankruptcy, national in its character, ought to be capable of execution in the national tribunals, without dependence upon those of the States in which it is possible that embarrassments might arise. The question has been quite fully and satisfactorily discussed by a member of this court in the first circuit, in the case of *Sherman v. Bingham*, . . . and we concur in the opinion there expressed.

Id. at 518; *see also Babbitt v. Dutcher*, 216 U.S. 102, 110-11 (1910) (following *Lathrop* and *Sherman*).

In *In re Wood*, 210 U.S. 246 (1908), the Court considered the procedures employed by the bankruptcy court in reviewing the debtor's transfer of property to his counsel prior to commencing his bankruptcy case. Under applicable law, the bankruptcy court could undo the transfer under certain conditions, thus bringing the transferred property into the estate. 210 U.S. at 253. In concluding that the bankruptcy court could conduct the adjudication, the Court observed: "Congress has the right to establish a uniform system of bankruptcy throughout the United States; and, having given jurisdiction to a particular district court to administer and distribute the property, it may, in some proper way, in such a case as this, call upon all interested to appear and assert their rights." *Id.* at 254.

In a series of decisions, the Court also has recognized that the essential, core functions of the nation's bankruptcy law are binding upon the States irrespective of their consent, and, further, that "we have previously endorsed individualized determinations of States' interests within the federal courts' *in rem* jurisdiction." *Hood*, 541 U.S. at 450. In doing so, the Court has indicated that a central reason for this conclusion is that, as the uniformity requirement itself indicates, bankruptcy law demands the uniform administration against all creditors of a collective proceeding that affects the rights of many parties, including state agencies. If all creditors were not bound to the proceeding, it would not be possible to administer it in a systematic fashion consistent with the fundamental goals of bankruptcy law and the Bankruptcy Clause itself. *See Railway Labor Executives' Ass'n v. Gibbons*, 455 U.S. 457, 472 (1982) ("The Framers sought to provide Congress with the power to enact uniform laws on the subject [of bankruptcies] enforceable among the States.").

For example, in *Irving Trust* the Court considered Congress's authority to divide a bankruptcy estate among creditors and deny the State of New York a share unless the State complied with applicable bankruptcy procedures. Concluding that Congress had such authority, the Court quoted from its prior decision in *Wood*, reiterating that "Congress has the right to establish a uniform system of bankruptcy throughout the United States; and having given jurisdiction to a particular district court to administer and distribute the property, it may, in some proper way, in such a case as this, call upon all interested to appear and assert their rights." *Irving Trust*, 288 U.S. at 332 (quoting *Wood*, 210 U.S. at 254). Again, the Court reasoned that otherwise it would not be possible to administer the bankruptcy estate consistent with the fundamental goals of bankruptcy law. *Irving Trust*, 288 U.S. at 333.

Similarly, in *Van Huffel*, the Court considered whether a bankruptcy court had the authority to sell property free and clear of the State's lien for unpaid taxes. In concluding that it does, the Court explained that the collection and distribution of the debtor's property is an essential function of bankruptcy law, and that "[r]ealization upon the lien created by the state law must yield to the requirements of bankruptcy administration." *Van Huffel*, 284 U.S. at 228; *see also Gardner*, 329 U.S. at 576 ("[B]oth in receivership cases, . . . and in bankruptcy cases, . . . the authority of the court to deal with the lien of a State has long been recognized. In reorganization cases the task of resolving disputes as to liens is a common one for the court.") (citations omitted). As in *Irving Trust*, the Court in *Gardner* explained that the ability of the bankruptcy court to deal with a State's tax lien was essential to maintaining the integrity of the process:

> If the reorganization court lacked the power to deal with tax liens of a State, the assertion by a State of a lien would pull out chunks of an estate from the reorganization court and transfer a part of the struggle over the corpus into tax bureaus and other state tribunals. That would . . . seriously impair the power of the court to administer the estate . . . It is the exclusive jurisdiction of the reorganization court which gives it power to preserve the [debtor] as a unit and as a going concern to prevent it from being divided up and dismembered piece-meal. Only in that way can continuous operation of the [debtor] be assured and a plan of reorganization be effected which not only safeguards the interests of the various claimants but is also compatible with the public interest.

Gardner, 329 U.S. at 473-74 (citations omitted).

In *Hood*, the Court extended the analysis to the question of the debtor's discharge, stating that "[u]nder our longstanding precedent, States, whether or not they choose to participate in the proceeding, are bound by a bankruptcy court's discharge order

no less than other creditors." 541 U.S. at 448; *see also Stellwagon v. Clum*, 245 U.S. 605, 613 (1918). Obviously, if a State were not so bound, the effectiveness of the bankruptcy system of discharge would be seriously impaired, if not destroyed altogether.

As this Court's precedents reveal, the uniformity requirement encompasses not one but numerous manifestations that replace or impair the prerogatives of the States, or that recognize in Congress authority that is affirmatively denied the States elsewhere in the Constitution. *See Pinkus*, 278 U.S. at 265 ("The national purpose to establish uniformity necessarily excludes state regulation."); *Stellwagon*, 245 U.S. at 613; *Moyses*, 186 U.S. at 188 ("The subject of 'bankruptcies' includes the power to discharge the debtor from his contracts and legal liabilities, as well as to distribute his property. The grant to Congress involves the power to impair the obligation of contracts, and this the states were forbidden to do."); *Ogden v. Saunders*, 25 U.S. 213 (1827) (state law could not discharge debt owed to citizen of another State); *Sturges*, 17 U.S. at 208 ("the act of the state of New York . . . so far as it attempts to discharge this defendant from the debt . . . is contrary to the constitution of the United States"). In this case, the relevant manifestation is that Congress is entitled to establish a uniform proceeding governing the determination of title to property that Wallace transferred to Petitioners, and to require that the property, or its value, be transferred to the estate if Wallace's transfer is avoided under section 547. Just as the States are bound by other aspects of a bankruptcy court's authority, they are bound in this case regardless of their consent because otherwise the reach of the preference rules would not be uniform and States would escape a critical component of the bankruptcy law.

3. Under the plan of the convention, the States surrendered their sovereignty to disregard the administration of bankruptcy cases, including the authority to determine questions of title and recover property.

As the Court has indicated, "immunity from suit is a fundamental aspect of the sovereignty which the States enjoyed before the ratification of the Constitution, and which they retain today . . . *except as altered by the plan of the Convention* or certain constitutional amendments." *Alden*, 527 U.S. at 713 (emphasis added). As explained above, the unique nature of a bankruptcy court's jurisdiction and functions, combined with the uniformity requirement of the Bankruptcy Clause, compel the conclusion that Petitioners are bound in this case to application of the Bankruptcy Code's preference rules. This is bolstered by evidence from the historical record, including THE FEDERALIST PAPERS.

As the Court stated in *Cohens*: "The opinion of the Federalist has always been considered as of great authority. It is a complete commentary on our constitution . . . . Its intrinsic merit entitled it to this high rank; and the part two of its authors performed in framing the constitution, put it very much in their power to explain the views with which it was framed." 19 U.S. at 418; *see also Printz v. United States*, 521 U.S. 898, 918-21 (1997); *Seminole Tribe*, 517 U.S. at 54, 69, 70 n.13.

In THE FEDERALIST NO. 81, Hamilton discussed sovereign immunity as follows:

> It is inherent in the nature of sovereignty, not to be amendable to the suit of an individual *without its consent*. This . . . exemption, as one of the attributes of sovereignty, is now enjoyed by the government of every state in the union. Unless, therefore, there is a surrender of this immunity in the plan of the convention, it will remain with the states, and the

> danger intimated must be merely ideal. The circumstances which are necessary to produce an alienation of state sovereignty, were discussed in considering the article of taxation, and need not be repeated here.

THE FEDERALIST NO. 81, at 422 (Alexander Hamilton) (George W. Carey & James McClellan eds., 2001). The article on taxation to which Hamilton refers is THE FEDERALIST NO. 32:

> But as the plan of the convention aims only at a partial Union or consolidation, the State Governments would clearly retain all the rights of sovereignty which they before had, and which were not, by that act, exclusively delegated to the United States. This *exclusive* delegation, or rather this alienation of state sovereignty, would only exist in three cases: where the constitution in express terms granted an exclusive authority to the union; where it granted, in one instance, an authority to the union, and in another, prohibited the states from exercising the like authority; and where it granted an authority to the union, to which a similar authority in the states would be absolutely and totally *contradictory* and *repugnant*.

THE FEDERALIST NO. 32, at 155 (Alexander Hamilton). Hamilton offered naturalization as an example of this third form of alienation of sovereignty: "The third will be found in that clause, which declares that Congress shall have power 'to establish a UNIFORM RULE of naturalization through the United States.". THE FEDERALIST NO. 32, at 155 (Alexander Hamilton). Hamilton explained that the power to make "uniform" laws "must necessarily be exclusive; because if each State had power to prescribe a DISTINCT RULE, there could be no UNIFORM RULE." THE FEDERALIST NO. 32, at 155 (Alexander Hamilton).

Like the power to enact "uniform" rules of naturalization, the Constitution vests in Congress the power to enact uniform bankruptcy laws. In this case, the ability of a state agency to disregard the jurisdiction of a bankruptcy court over preferential transfers constitutes a distinct state rule at odds with the uniform rule of bankruptcy law. A transfer of property avoided under section 547 is preserved for the benefit of the estate under section 551; must be returned under section 542; and may be recovered under sections 550. As explained above, application of these provisions does not involve a suit by a private citizen against an un-consenting State for the violation of some state law entitlement. On the contrary, the application of these provisions fulfills the command of federal bankruptcy law over the determination and disposition of property of the bankruptcy estate. Under the plan of the convention, state agencies must yield to the federal power to decide what property belongs to the estate and to the administration of the estate.

As the Court has observed, "the framers of the Constitution were familiar with . . . the bankrupt laws of England." *Hanover Nat'l Bank of the City of New York v. Moyses*, 186 U.S. 181, 187 (1902). In England, the recovery of voidable preferences has a long history that predates the Constitutional Convention. Lord Coke first explained the basic concept in 1584 and its central premise of equality of distribution. *See The Case of Bankrupts*, 76 Eng. Rep. 441 (K.B. 1584) ("it would be unequal and unconscionable, and a great defect in the law, if, after that he hath utterly discredited himself by becoming a bankrupt, the law should credit him to make distribution of his goods to whom he pleases"). By 1758, the recovery of preferential transfers in a manner similar to that prescribed by the Bankruptcy Code had become established law. *See Worsely v. DeMattos*, 1 Burr. 467, 482, 96 Eng. Rep. 1160 (K.B. 1758) (Mansfield, J.) (a debtor's voluntary payment to a creditor, not in the regular course of business, was "void with respect to the other creditors"). During the colonial era, different States likewise experimented with preference laws. *See* Peter J. Coleman, DEBTORS AND CREDITORS IN AMERICA:

INSOLVENCY, IMPRISONMENT FOR DEBT, AND BANKRUPTCY, 1607-1900 69, 212 (1974) (discussing Vermont and Delaware laws); F. Regis Noel, A HISTORY OF THE BANKRUPTCY LAW, 43-44 (2002) (discussing Maryland law); Thomas E. Plank, *Bankruptcy and Federalism*, 71 Fordham L. Rev. 1063, 1086-87 (2002) (discussing Maryland law). The concept of a preferential recovery is thus not a recent invention, but rather has existed as part of the larger fabric of bankruptcy law for many centuries.

Moreover, that Congress understood from the very beginning that exercise of the Bankruptcy Power could abrogate the rights of the States is also evidenced by the first Bankruptcy Act of 1800, which vested the district courts with broad subject matter jurisdiction over bankruptcy cases. *See* 2 Stat. 164, section 11. Congress specifically provided in section 62 of the first Act that "[n]othing contained in this law shall, in any manner, affect the right of preference to prior satisfaction of debts due to the United States as secured or provided by any law heretofore passed, nor shall be construed to lessen or impair any right to, or security for, money due to the United States or to any of them." 2 Stat. 19 (repealed 1803, 2 Stat. 248). If Congress did not understand that the rights of the States could properly be adjusted, there would have been no need for this provision. Indeed, commenting on section 62 in 1805, this Court explained that the section was designed "to retain the right of the United States in their existing situation, whatever that situation may be." *United States v. Fisher*, 6 U.S. 358, 394 (1805).

Finally, the concept that a bankruptcy court may enforce its jurisdiction over property that should be included as part of the estate by requiring the turnover of property out of the hands of governmental officials is bolstered by the fact that the Act of 1800 also authorized habeas relief: debtors under the Act were entitled to an order directing their release from prison if incarcerated on account of a discharged obligation. Act of 1800 at § 38, 2 Stat. 32 ("[I]f any bankrupt, who shall have obtained [a certificate of discharge], shall be taken in execution or detained in prison, on account of any debts owing before he became a

bankrupt . . . it shall be lawful for any of the judges of the court wherein judgment was so obtained, or for any court, judge, or justice, within the district in which such bankrupt shall be detained, having powers to award or allow the writ of *habeas corpus*, on such bankrupt producing his certificate so as aforesaid allowed, to order any sheriff or gaoler who shall have such bankrupt in custody, to discharge such bankrupt without fee or charge."). Just as a bankruptcy court may require the turnover of the debtor himself out of state custody in the exercise of its essential bankruptcy jurisdiction, it may also require from a state agency the turnover of his property to be administered as part of the federally created bankruptcy estate.

CONCLUSION

For the foregoing reasons, the Court should affirm the decision of the Court of Appeals.

Respectfully submitted,

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